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C O N F I D E N T I A L SECTION 01 OF 02 SHANGHAI 000380

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TAGS: [PGOV](#) [PINR](#) [EINV](#) [ECON](#) [CH](#)
SUBJECT: CARLYLE, XUGONG, AND BUREAUCRATIC POLITICS

REF: A) 06 BEIJING 16050

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CLASSIFIED BY: Kenneth Jarrett, Consul General, U.S. Consulate,
Shanghai, Department of State.
REASON: 1.4 (b), (d)

11. (C) Summary: Central government officials promised a resolution to Carlyle Group's effort to purchase a 45 percent stake--down from its initial 85 percent bid--in Xugong Machine Group by the end of July. The current hang-up was the result of bureaucratic infighting between the Ministry of Commerce (MOFCOM) and the powerful National Development and Reform Commission (NDRC). While NDRC had no specific objections to the deal, it had decided to flex its bureaucratic muscles vis a vis MOFCOM in a bureaucratic fight over control over the investment process. End summary.

Carlyle-Xugong Deal: An End Finally in Sight

12. (C) During a June 20 discussion with Pol/Econ Chief and Poloff, Carlyle's Chief China representative Luo Yi (strictly protect) said that the Chinese government had promised a resolution of the approval process for Carlyle's bid to acquire a 45 percent stake in Xugong Machine Group by the end of July. He said that in January, Carlyle had revised its offer to purchase an interest in Xugong from its original October 2005 bid of 85 percent, after running into pushback from bureaucratic interests (Ref A).

A Hostage to Infighting

13. (C) Luo explained that MOFCOM had sent a report to the State Council in early May recommending approval. The State Council then sent out letters to other relevant ministries seeking their input. The China Securities Regulatory Commission, the State Asset Supervision Administration Commission, the Tax Bureau, the State Administration of Industry and Commerce, and the State Administration for Foreign Exchange all responded recommending approval of the deal. However, NDRC, although it had no

specific objection to the deal itself, ordered negotiations put on hold, citing objections over the investment review and approval process. NDRC said it should be the entity responsible for approving the deal rather than MOFCOM.

14. (C) Despite MOFCOM objections, NDRC forced Carlyle and Xugong back to the negotiating table. Luo said that Carlyle was tired of being punted around like a political football while the ministries fought over who had control of the deal and the investment approval process generally. However, he had been informed by both NDRC and MOFCOM that pulling out now was not an option and that a final decision would be made in July. To pull out would make both ministries lose face and jeopardize Carlyle's relationship with them. When pressed, however, Luo admitted that even with all of the headaches, the deal would still be "very profitable." He expressed hope that Treasury Deputy Secretary Kimmitt's recent visit to Beijing might help force a bit more transparency and movement in China's investment approval process.

The NDRC Juggernaut

15. (C) Luo said that this current struggle highlighted the immense power that NDRC held, despite efforts by former Premier Zhu Rongji to dissipate its clout. Even in cases where it had no clear stake, such as the Xugong deal, NDRC would get involved to remind other ministries that it was still the preeminent economic organization in the State Council. Its top position was highlighted by the fact that in such cases, the State Council did nothing to intervene against NDRC's actions. Luo believed that the difficulties Carlyle had experienced with MOFCOM and NDRC had little to do with personal politics between their ministers, and more to do with bureaucratic infighting.

16. (C) According to Luo, part of NDRC's clout resulted from the close ties between NDRC Chairman Ma Kai and Premier Wen. They had formed a relationship when Ma had worked for Wen in the

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State Council when Wen was Vice Premier. Luo assessed that Ma was being groomed by Wen to backfill the Premiership when Wen retired in 2012 (Note: Luo is friends with Ma's daughter and her husband. End note.). Commenting on MOFCOM Minister Bo Xilai, Luo said that he was widely disliked by his peers, primarily because they disliked his father, Bo Yibo, a once-powerful and now-deceased party elder. Luo assessed that despite his unpopularity, Bo might still rise to the level of vice premier, but had little hope of ever becoming Premier.
JARRETT